OUT-OF-COURT RESTRUCTURING GUIDELINES FOR MAURITIUS

1. INTRODUCTION

It is a generally accepted global principle that restructurings achieved outside formal insolvency proceedings yield higher stakeholder returns for those involved, as these are more flexible and efficient than court proceedings.

Consequently, before an insolvency case is brought to court one option available to the debtor and creditors involved is an informal workout, or out-of-court restructuring, where both the debtor and the creditor(s) attempt to come to a private arrangement for the adjustment of the terms of the debt and to allow the debtor to continue normal business operations.

It is generally accepted that out-of-court workouts:

- Allow viable businesses to continue to operate and to emerge successfully from financial distress;
- Allow creditors generally, but specifically lenders, to reduce losses;
- To a large extent avoid the social and economic impact of major business failures’
- Reduce pressure on the courts;
- Better serve other key stakeholders, such as customers, employees, suppliers and investors, since businesses subject to out-of-court restructuring proceedings continue to trade;
- Are more efficient and effective than court procedures due to the shorter time frames and higher recovery rates;
- Assist the commercial community in developing confidence in the fairness, transparency and accountability of insolvency and restructuring proceedings;
- Can apply to any form of business enterprise.

The approach taken in these guidelines is that of INSOL International’s “Statement of Principles for a Global Approach to Multi-Creditor Workouts”. The INSOL principles are highly regarded around the world, and have formed the basis for out-of-court restructuring guidelines in various jurisdictions.

2. OBJECTIVES AND SCOPE OF THESE GUIDELINES

These guidelines are intended to provide business entities (debtors), creditors and government agencies with guidance for out-of-court restructurings.
The principles contained in these guidelines, and the guidance notes for the implementation of the principles, are aimed at providing debtors and their creditors with a framework based on international best practices in this field.

The principles contained in this guide may also be used, to the extent that they are compatible, in steering negotiations between the debtor and the creditors in formal restructuring mechanisms contained in the Insolvency Act 2009.

3. **KEY CONCEPTS AND TYPES OF CREDITOR WORKOUTS**

3.1 **Expected Outcomes**

The expected outcome is a negotiated restructuring plan between the debtor and the relevant creditors, allowing the debtor’s business to continue and to ensure the total or partial coverage of its debt (“relevant creditors” are usually creditors having the largest claims, or those crucial to the continuation of the business of the entity; these creditors will usually be the debtor’s bankers, but it may also include other major creditors such as financing creditors, landlords and major suppliers). Should a negotiated restructuring plan not materialize, the possible alternatives are the commencement of pre-insolvency court proceedings (such as a scheme of arrangement), or formal insolvency proceedings. Whatever the outcome, the use of the information collected during the out-of-court workout process may lead to expedited formal proceedings.

3.2 **Types of Creditor Workouts**

Workout negotiations may be:

- Bilateral negotiations between the debtor and a creditor, leading to the rescheduling of payments and/or debt forgiveness;
- Multilateral negotiations between the debtor and its major creditors, leading to debt rescheduling, debt forgiveness or the granting of other incentives, as agreed by the parties.

3.3 **Difference Between Out-of-Court Workouts and Formal Restructuring Proceedings**

The most important differences between out-of-court workouts and formal insolvency proceedings are:

- Out-of-court workouts do not seek to vary existing entitlements or bind non-consenting creditors;
- Out-of-court workouts are consensual and do not threaten or compromise the existing legal rights of the debtor and creditors;
- Both the process adopted as well as the arrangements between the debtor and its creditors in an out-of-court workout are flexible, may be achieved in a shorter period of time and with a lower risk relating to the debtor’s business reputation when compared to formal insolvency proceedings;
- Out-of-court proceedings allow a more favourable context for obtaining
additional finance.

4. PRINCIPLES FOR OUT-OF-COURT RESTRUCTURING GUIDELINES IN MAURITIUS

FIRST PRINCIPLE
Where a debtor finds itself in financial distress, all relevant creditors should be prepared to co-operate with each other, and the debtor, to provide sufficient (though limited) time – the “Standstill Period” - for information about the debtor to be obtained and evaluated, and for proposals for resolving the debtor’s financial difficulties to be formulated and assessed, unless in a particular case such a course is inappropriate.

Guidance Notes:
No debtor has a right to a Standstill Period in order to conduct an out-of-court workout: this is a concession by creditors, and not a right of the debtor. The debtor, of its own accord or through its advisers, needs to assess whether there is a realistic possibility that its financial difficulties can be resolved with a view to its long-term viability. If restoring the long-term viability of the debtor is not possible, alternative remedies, such as the liquidation of the debtor by way of formal insolvency proceedings, should be considered.

The purpose of the Standstill Period is to provide the debtor with sufficient time to prepare a restructuring plan that will resolve the debtor’s financial difficulties. The restructuring plan must demonstrate that the distressed business is capable of operating profitably, as well as the extent to which it will be able to repay its debts. There is no prescribed minimum information that the restructuring plan should contain, but it is imperative that the plan should demonstrate that there is a reasonable prospect of the business becoming viable in the foreseeable future. Matters normally dealt with in a restructuring plan would include the following:

- Projected trading profit and loss for the foreseeable future;
- Cash flow forecasts;
- Sources of additional capital;
- Any proposed modification of creditors’ rights (for example by deferral, variation or debt forgiveness);
- Significant changes in management or ownership.

The reference to all “relevant creditors” refers to those creditors whose rights will be affected by the proposed restructuring contained in the plan.
The unanimous support of all relevant creditors is essential. The number of participating creditors should therefore be kept to a minimum in order to reduce the complexity of the negotiations. If support for the plan by creditors is inadequate, the restructuring will be unable to go ahead.

The manner in which this principle is expressed makes it clear that what is hoped will develop over time is a willingness by creditors to participate in an out-of-court restructuring as a matter of course, unless such a course of action is clearly inappropriate in the circumstances.

The Standstill Period should be limited to the time that is required to produce a viable restructuring plan, or to determine that such a plan cannot be produced within an acceptable time limit. The Standstill Period will vary from case to case, although usually it should not be longer than a few weeks.

During the Standstill Period, it is vital that the relevant creditors receive adequate reliable information to enable them to assess the debtor’s financial position, to understand what has caused the underlying financial problems, and to evaluate any proposed solutions that are put forward. It must be borne in mind that at the conclusion of the negotiating process, the relevant creditors will be requested to approve the proposed solution. If the relevant creditors do not have absolute confidence that they have received adequate and accurate information, as well as sufficient time to review it, they will not be in a position to approve the proposed course of action.

One of the greatest challenges facing an out-of-court restructuring plan is the tendency of individual creditors to try and pressure the debtor for payment. The greater the likelihood of such payments being made, the smaller chance there will be of the restructuring plan succeeding.

SECOND PRINCIPLE
During the Standstill Period, all relevant creditors should agree not to take any steps to enforce their claims against, or to reduce their exposure to, the debtor (this would exclude the disposal of their debt to a third party). However, creditors are simultaneously entitled to expect that their position relative to other creditors will not be prejudiced during the Standstill Period.

Guidance Notes:
The aim of this principle is to achieve stability among creditors during the Standstill Period, and to maintain the status quo regarding their claims as they existed immediately prior to the Standstill Period. However this may achieved, all relevant creditors must be comfortable and confident that in deciding not to pursue their individual enforcement remedies, they will not be prejudiced in relation to other creditors should a consensual
way forward for the debtor not be found. Each creditor’s ranking relative to the other creditors must be neither worsened nor improved during the workout process.

The appeal of the out-of-court restructuring process can be greatly enhanced by the involvement of qualified professional advisers (where these are available), or government agencies that have moral authority and who can earn the respect of the creditors. In the context of Mauritius there is an important role for the Bank of Mauritius, the Mauritius Bankers Association and the Insolvency Service in not only sponsoring and promoting the out-of-court restructuring guidelines, but also by publicly or formally endorsing them.

Although a written agreement for a Standstill Period is not necessary in cases where an effective informal understanding amongst the relevant creditors exists, in those cases where the Standstill Agreement has been reduced to writing it is necessary for the creditors signing up to the agreement to agree that, during the Standstill Period, they will:

- Not to try to improve their positions relative to other creditors;
- Not insist on payment of amounts owing to them;
- Not initiate collection, security enforcement or liquidation proceedings; and
- Allow existing credit lines and facilities to be used.

**THIRD PRINCIPLE**

During the Standstill Period, the debtor should not take any action that would adversely affect the prospective returns to the relevant creditors on a collective or individual basis, as compared to their position at the commencement of the Standstill Period.

**Guidance Notes:**

If the creditors agree individually or collectively that they will not take any steps intended to gain an advantage over other creditors, it follows that the debtor must also agree not to do anything that would be detrimental to the interests of any creditor or class of creditors, or alter their respective priority positions from the commencement of the Standstill Period.

One important exception to this principle is the ability of the debtor to continue to make payments in what is commonly referred to as “the ordinary course of business”. If this exception were not allowed, the debtor would not be able to continue to trade while attempts are made to agree the terms of a workout. The types of issues that should be avoided here are for example transactions that are not for full value, the making of preferential payments, the granting of security for previously unsecured debts, or incurring new loans without prior creditor consent.
**FOURTH PRINCIPLE**

In an out-of-court restructuring, the interests of the relevant creditors are best served by coordinating their response to a debtor experiencing financial difficulties. In complex cases coordination of this nature may be facilitated by the formation of one or more representative coordination committees, by the appointment of professional advisers to advise and assist such committees and, where appropriate, the relevant creditors themselves participating in the process as a whole.

**Guidance Notes:**
All negotiations between the debtor and the relevant creditors must be conducted in the utmost good faith, in an atmosphere of honesty and frankness, and with the objective of finding a constructive solution to the debtor’s financial problems. If any of the parties lose confidence in the fact that their counterparts are negotiating in good faith, the negotiations to find a constructive solution are likely to fail which will in turn lead to the relevant creditors falling back on their legal remedies of enforcement and / or the commencement of insolvency proceedings.

Due the number of different creditors that could be involved in an out-of-court restructuring agreement, and their different priority positions in the event of a liquidation, it is often advisable for committees to be formed and for professional advisers to play their part in achieving consensus on the terms of the restructuring agreement. It may be appropriate for the costs of outside advisers, perhaps within specified limits, to be paid by the debtor.

Relevant creditors, or a representative co-ordination committee, may wish to consider appointing one person to lead negotiations with the debtor on their behalf (this could for example be the creditor with the greatest exposure, one with experience in managing restructuring negotiations, or an independent person).

In cases where the relevant creditors are experiencing difficulties in reaching consensus, it may be appropriate to consider whether or not some form of alternative dispute resolution, such as mediation, could be used to reach agreement. Any agreement reached on this basis can be made conditional on an overall restructuring plan being agreed which includes them.

**FIFTH PRINCIPLE**

During the Standstill Period, the debtor should provide all relevant information regarding its assets, liabilities, business and future prospects. All relevant creditors and/or their professional advisers should be given reasonable and timely access to this information in order to enable a proper evaluation to be made of its financial
position, and for the formulation of any proposals that are to be made to the relevant creditors.

Guidance Notes:

The integrity of the restructuring process will largely depend on the quality of the information in the possession of the creditors being asked to compromise their debts. Although time will be of the essence in most restructuring cases, the Standstill Period must be sufficiently long in order for the necessary information regarding the debtor to be gathered, distributed and understood by all the parties concerned. The relevant creditors must also be provided with sufficient time to consider the details of the restructuring proposal.

In order for the process to have integrity, the debtor must be subject to strict obligations regarding disclosure. At the very least, the information provided must include full particulars of the debtor’s assets and liabilities, as well as the future business prospects of the debtor. In order to produce information relating to the future business prospects of the debtor, forecasts and projections that are more detailed than those it would normally prepare, will likely have to be prepared.

**SIXTH PRINCIPLE**

Proposals contained in a restructuring plan for resolving the financial difficulties of the debtor, and, in so far as this is practicable, arrangements between the relevant creditors relating to any Standstill Period, must comply with both the applicable law as well as reflect the relative positions of the relevant creditors at the commencement of the Standstill Period.

Guidance Notes:

In the absence of special circumstances, the relevant creditors will expect to be treated in the same way as creditors in a similar position to themselves, both during the negotiation process and in any proposed restructuring plan.

The provisions of the domestic or local law, including the insolvency law, should serve as a guide to the relative priority position of creditors. In more complex cases, relevant creditors will appreciate that it may be necessary for minor trade creditors to be paid in full in order to achieve greater consensus, and also to allow the debtor’s business to continue.
SEVENTH PRINCIPLE

Any information obtained for the purposes of the restructuring process dealing with the assets, liabilities and business of the debtor, as well as any proposals for resolving its financial difficulties, should be made available to all the relevant creditors and should, unless already in the public domain, be treated as confidential.

Guidance Notes:

Ideally, all relevant creditors should be provided with exactly the same information. This information should be as detailed as the circumstances of each case requires, but it must in any event be sufficiently detailed to permit creditors to form their own view of the merits of the restructuring proposal being put forward by the debtor.

If in any given case information is price-sensitive, or in some way the subject of legitimate confidentiality concerns, then confidentiality agreements are commonly required before the information is made available.

In complex cases the issue of debt trading may arise. This raises complex issues and special conditions may be needed where creditors intend to trade their debt.

EIGHTH PRINCIPLE

If additional funding is provided to the debtor during the Standstill Period, or as part of any restructuring proposal, the repayment of such additional funding should, in so far as this practical, be accorded priority status as compared to other indebtedness or claims of the relevant creditors that existed at the time of the commencement of the Standstill Period.

Guidance Notes:

The ability of the debtor to continue in business during any period of negotiation is central to the success of an out-of-court restructuring. While some debtors may not need to depend on third party financing to continue operating, there are many that do. In such an event, or where additional funding is required for other justifiable reasons during the restructuring process, the sources are typically the proceeds of the sale of non-core assets, new investment from shareholders, or additional lending from existing creditors (including banks).

Unless a certain degree of priority is accorded to any additional lending, it is highly unlikely that financing will be made available, and the workout may fail to survive long enough to permit a restructuring plan to be fully developed and considered by the relevant creditors.
The priority treatment accorded to additional financing made available in this way is often referred to as a “super priority” since the provider of such finance is entitled to be paid in priority to the claims of pre-existing creditors, even if the workout eventually fails and formal insolvency follows. It is usually only because of the existence of this priority that existing creditors are willing to provide this form of finance. It is seen as a relatively low risk manner of increasing the chances that their existing obligations will be satisfied, if only in part, in the long term.

There are many ways of achieving the desired priority for new lenders, including the provision of fresh security of some kind (for example a first ranking mortgage security over physical assets or receivables), and various forms of statutory priority. Care must be taken to ensure that any security will be valid in the event of the insolvency of the debtor.

21 January 2013
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